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C O N F I D E N T I A L SECTION 01 OF 02 BAGHDAD 000210

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TAGS: ECON EFIN ENRG EPET ETRD PGOV PREL TU IZ
SUBJECT: MINISTER OF FINANCE ALLAWI ADDRESSES FUEL IMPORT CRISIS

REF: A. A) ANKARA 278
¶B. B) DELARE-GOLDBERGER JAN 22-23 EMAILS/TELECONS

Classified By: Economic Minister Counselor Tom Delare for reasons 1.4 (b) and (d).

¶1. (C/REL GBR AUS) Summary: Minister of Finance (MoF) Ali Allawi said that he has a green light from the Council of Ministers to offer the Turks a plan by which Iraq will pay off its arrears over a 12-month period, at an interest rate of 3%-4%. He said Iraq will commit to keeping its 2006 imports within budget, with SOMO (the State Oil Marketing Organization) empowered to pay suppliers only/only via approved Letters of Credit through the Trade Bank of Iraq (TBI). As this volume of imports will not meet current consumption in Iraq, Allawi predicted that rationing is inevitable and asked for U.S. assistance in developing an equitable system. Allawi hopes to use the crisis to push for legislation opening the import and sale of fuel to private companies. End Summary.

Allawi's Repayment Plan

¶2. (C/REL GBR AUS) Minister of Finance (MoF) Ali Allawi told Economic Minister Counselor January 22 that the Council of Ministers had approved a plan to offer repayment to Turkish fuel suppliers staggered over a 12-month period. To make the arrangement more palatable, Allawi said the that the GOI would be prepared to offer a "reasonable" rate of interest - perhaps in the 3-4% range. As part of this arrangement, the GOI seeks to secure agreement from Turkish suppliers that no/no further shipments of petroleum products will be made without a Letter of Credit (through the Trade Bank of Iraq) or formal MoF agreement to cover the cost of the shipment. In the event of an emergency, additional fuel above the budgeted $250 million/month limit may be imported, but Allawi averred that a decision of the Council of Ministers will be required to make that happen. Allawi said that MoF has tried to enforce discipline of this sort on the Ministry of Oil (MoO) and its purchasing arm, the State Oil Marketing Organization (SOMO) since last October, totally without success. Given current budget difficulties, Allawi sees it as imperative to hold fast to a tough position now.

¶3. (C/REL GBR AUS) Average monthly purchases of imported fuel rose and fell throughout 2005, but averaged out around $400 million/month -- $150 million/month over that allocated in this year's budget. According to rough numbers offered by Allawi, after liquidation of current arrears of some $880 million, the GOI will have only just over $2 billion available for fuel purchases for the remainder of the year.

That will permit purchases at only about 40% of last year's level (Note: This does not factor in possibly higher prices for petroleum products. End Note). The Embassy estimates that as much as half of all imported fuel goes to generate electricity, leaving the GOI with a stark choice: Do they attempt to keep the grid up and running or do they direct some portion of the limited fuel imports to automotive and other uses, thereby contributing to a further fall-off in electricity generation. Allawi is concerned that the government will have to quickly launch a rationing or coupon scheme to permit consumer purchases of imported fuel. He asked our advice on how to implement a workable rationing system and establish priorities. He said he is concerned that the government will have to quickly launch a rationing or coupon scheme to permit consumer purchases of imported fuel. He asked our advice on how to implement a workable rationing system and establish priorities.

Opening Up the Downstream Fuel Market?

¶4. (C/REL GBR AUS) On a brighter note, Allawi said he sees an opportunity to use the current crisis to secure an opening of the downstream retail market. In a separate conversation January 21, Allawi's Chief of Staff told us that MoF officials are convinced that prevarication on the part of the Ministry of Oil and its allies within the PM's office prevented a bill opening up the retail fuel sector from ever reaching Parliament for action. Allawi said that he still views the legislation as an essential first step to getting the government out of the business of fuel imports. It will begin making headway to reduce costly subsidies, since sales

of privately imported fuel would be at market rates. EconMinCouns stressed that the bill, when re-introduced, be amended to clearly authorize retail outlets to operate without state control of their profit margins, an essential element to attract potential importers that is vague in the existing draft. Allawi hopes to urge Prime Minister Ja'fari to recall the Transitional National Assembly (TNA) in an extraordinary session to get action on the fuel import bill, although he confessed that he had not yet broached this subject with the PM (See SEPTEL for additional information on this subject from Deputy Prime Minister Chalabi.)

MoF Requests Embassy Assistance

¶5. (C/REL GBR AUS) Allawi asked for U.S. assistance in floating his plan in Ankara before sitting down with the Turkish Ambassador in Baghdad (Note: Baghdad Econ has been in direct contact with Ankara Econ via email and phone. End Note). Regarding next steps, Allawi said that the government would move to establish a joint Ministry of Finance-Ministry of Oil Task Force, on which he implied that he would welcome USG involvement. Post will follow up on both the task force as well as assisting MoF, if and when they develop their rationing scheme.

¶6. (C/REL GBR AUS) Comment: It may be that this strategizing on the part of MoF to use the crisis to open up the downstream retail market and introduce rationing will be quashed by PM Ja'fari. The country is in a bone fide fuel crisis and some cool nerve would be required to play this hand within the bureaucracy. Regardless of possible Turkish or Kuwaiti disgruntlement, the goal desired by the Ministry of Finance is a good one. There is a desperate need to shift the country away from the enormous subsidy payments entailed by the current importation and discounted sale of fuel products. Opening up even a part of the petroleum sector promises to improve services, cut back on corruption, as well as save budget funds.

¶7. (C/REL GBR AUS) Comment cont'd: Under Allawi's plans, rationing would need to start immediately - probably for all uses and/or the state will need to make larger allocations for fuel purchases. Given the current revenue streams, that would necessarily entail drawdown of capital budgets across the government - the only ready source of funds. Alternately, rapid movement to privatize the oil import market (the goal at the Ministry of Finance) would eliminate the need for rationing as private retail came on line, through true market prices being introduced at the gas pumps. This rather dire situation would also seem to reinforce the need to continue with subsidy elimination - as a means to free up scarce budget resources.
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